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Supreme Court of the United States

OCTOBER TERM, 1941.

No. 173.

GEORGE H. MASON, Trustee in Bankruptcy of Worcester Motor Co. Inc.,
Petitioner for Writ of Certiorari,

vs.

JOHN WYLDE *et al.*,
Respondents.

BRIEF FOR THE RESPONDENTS.

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LAWYERS' BRIEF & PUBLISHING CO.
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JOHN WYLDE *et al.*,
Respondents.

BRIEF FOR THE RESPONDENTS.

Summary and Short Statement of Matter Involved.

This was an action of "contract or tort" commenced by the petitioner, hereinafter called the plaintiff, by writ dated April 15, 1933, returnable to the Superior Court for Worcester County, Massachusetts. The plaintiff's declaration charged:

> "Count 1. The plaintiff is trustee in bankruptcy of Worcester Motor Co., Inc., and authorized to sue. The defendants converted to their own use the property of Worcester Motor Co., Inc., to wit, sixteen automobiles of the value of $5000.
>
> "Count 2. The plaintiff is trustee in bankruptcy of Worcester Motor Co., Inc., and authorized to sue. The

defendants being creditors of the Worcester Motor Co., Inc., did receive property of the Worcester Motor Co., Inc., to the value of $5000 within four months of the petition in bankruptcy being filed by the Worcester Motor Co. Inc., and that the defendants or their agents had reasonable cause to believe that Worcester Motor Co., Inc. was insolvent; that the giving and receiving of the property as herein stated created a preference in their behalf as against the other creditors of the bankrupt wherein they received a greater percentage than the other creditors of the same class.

"Count 3. The plaintiff is trustee in bankruptcy of Worcester Motor Co., Inc., and authorized to sue. The defendants in violation of the National Bankruptcy Act did receive goods of the bankrupt to the value of $5000 with intent to hinder and delay the other creditors.

"Count 4. The plaintiff is trustee in bankruptcy of Worcester Motor Co., Inc., and authorized to sue. The defendants owe him $4000 for moneys had and received.

"All counts for one and same cause of action."

The defendants' answer was a general denial. The case was referred to an Auditor who found for the defendants.

It was tried in the Superior Court on January 14, 1936, no evidence other than the Auditor's Report (Record, pp. 1-11) being introduced. On April 1, 1936 the Superior Court made a finding and order for judgment for the plaintiff. The defendants alleged exceptions which were sustained by the Supreme Judicial Court and judgment ordered for the defendants, which was entered in the Superior Court on March 17, 1941. On June 16, 1941 this petition for certiorari was filed. The facts as established by the Auditor's Report (Record, pp. 1-11) were as follows:

The petitioner is trustee in bankruptcy of Worcester Motor Co. Inc. which was adjudicated a bankrupt on August 5, 1932. The Worcester Motor Co. Inc. was en-

gaged in the business of buying, selling and dealing in motor vehicles until August 1, 1932, making use of moneys advanced by the defendants upon the security of the motor vehicles purchased, evidenced by written contracts called trust receipts in the form shown by Exhibit "A" attached to the Auditor's Report (Record, p. 6). The amounts so advanced amounted to approximately $100,000 in 1931 and approximately $50,000 in the first seven months of 1932. All moneys were advanced against security given by Worcester Motor Co. Inc. to the defendants co-incident with such advancements. Each contract or trust receipt stated that Worcester Motor Co. Inc. had received from Patterson, Wylde & Windeler, the owner thereof, a certain motor vehicle purchased under credit opened by them for its account, in consideration whereof it agreed to hold said motor vehicle in trust for the defendants as their property, and to return the same on demand, but with liberty to exhibit and only with the written consent of the defendants first obtained to sell the same for their account for cash for not less than the stated amount, and in case of sale to keep the proceeds separate from its funds and immediately hand them to the defendants. The defendants had the right to cancel the trust at any time and repossess the motor vehicle.

On July 22, 1932, trust receipts covering eleven used cars valued at $1,396.00 were substituted for trust receipts covering four new cars, which the Worcester Motor Co. Inc. had sold or contracted to sell, a part of the proceeds of those sales then being in the possession of Worcester Motor Co. Inc. and a part of the money so received having been expended by it in the usual course of its business. The defendants received and accepted the eleven used cars as security for the amounts advanced against the four motor

vehicles described in the trust receipts for which they were exchanged. The defendants then held similar trust receipts covering five new cars amounting to $2,270.00 which, with the eleven used cars, remained in the possession of Worcester Motor Co. Inc. until about August 1, 1932 when the eleven used cars and the five new cars were repossessed by the defendants and thereafter sold, the used cars for $1,396.00 and the new cars for $2,270.00, which was a reasonable price, and the defendants did not receive any sums in excess of the amounts due them under said trust receipts. The defendants acted in good faith and within the powers set forth in the trust receipts.

None of the trust receipts were recorded. They were valid as between the parties thereto, and no creditor or third person had acquired any rights in the motor vehicles before the defendants perfected their title by repossession. At the time of repossession Worcester Motor Co. Inc. was insolvent to the knowledge of the defendants, but it was solvent when the title to the motor vehicles was transferred to the defendants under the trust receipts, and there was no evidence of insolvency prior to the date of repossession, or that there were any other creditors of the same class. Each trust receipt was given as security for the purchase price of the motor vehicle which was bought with the money advanced by the defendants, and the assets of the company were not depleted by the giving of these trust receipts. Nothing was taken away from the creditors.

At the trial the defendants requested rulings that upon the pleadings and the evidence the plaintiff was not entitled to recover upon any count of his declaration. In sustaining the exceptions of the defendants to the finding and rulings of the trial court and ordering the entry of judgment for the defendants, the Supreme Judicial Court of Massachusetts held that the evidence did not sustain any count of the plaintiff's declaration.

Question Presented.

In the absence of any clear specification of errors alleged, the question seems to be whether one who advanced money to a solvent merchant in good faith, but within four months prior to bankruptcy, upon the security of the transfer of title to the merchandise purchased with that money, evidenced by trust receipts which are valid between the parties thereto under Massachusetts law although not recorded under the applicable chattel mortgage law, is guilty of a fraudulent preference if he perfects his title to his security by lawful foreclosure after the merchant becomes insolvent, but before any bankruptcy petition is filed or third persons acquire any rights in the merchandise.

In view of the averment on page 5 of the petition for certiorari that the recording of a chattel mortgage is required under Massachsetts law by the Bankruptcy Act, and the absence of any statement that under Massachusetts law an unrecorded chattel mortgage is valid as between the parties thereto, and if foreclosed before any creditor fixes a lien by attachment or taking on execution the title of the mortgagee is perfected and relates back to the time of the execution of the chattel mortgage, it becomes necessary to consider just what the Supreme Judicial Court actually decided, which was,—

That the so-called trust receipts were valid as between the parties thereto—Worcester Motor Co. Inc. and the defendants—from the time they were executed; that they were security instruments by which title to the automobiles passed to the defendants for security only, and were in substance chattel mortgages and were governed by the law applicable to chattel mortgages; that possession of the automobiles was taken by the defendants before the date of bankruptcy in accordance with the terms of the trust re-

ceipts, so that thereafter the automobiles were not held by the defendants as security, but the absolute property therein was in the defendants prior to the date of bankruptcy; that the title of the defendants to the automobiles was perfected by the defendants by their taking possession of the automobiles for foreclosure according to the terms of the trust receipts before date of bankruptcy; that the fact that the trust receipts were not recorded did not prevent the defendants from acquiring title to the automobiles thereunder prior to the date of bankruptcy as against the company if no rights of other persons had intervened, and that no rights of other persons had intervened.

That there was no conveyance of the automobiles to the defendants in fraud of creditors according to the principles of State law governing fraudulent conveyances, and no transfer made within four months prior to the date of bankruptcy which was void under U. S. C. Title 11, Section 107 (E), either because made with the intent and purpose on the part of the company to hinder, delay or defraud creditors, or because constituting a conveyance, transfer or encumbrance made by the company while insolvent, or which was voidable by the trustee under U. S. C. Title 11, Section 96 (B) because made within four months before the date of bankruptcy when the company was insolvent.

That on the facts found there was no conveyance of the automobiles to the defendants in fraud of creditors; that there was no intent to hinder, delay or defraud either present or future creditors; that each trust receipt was given as security for the purchase price of an automobile; that the assets of the company were not depleted by the giving of these trust receipts; that they took nothing away from the creditors; that the trust receipts relating to the eleven used automobiles were given in substitution for the original trust receipts for four new automobiles as security

for the original obligations, and that no agreement or understanding to withhold the trust receipts from record is shown.

That the defendants were purchasers in good faith and for a present fair consideration; that the time of the transfer by the law of the Commonwealth is the time of the giving of the security instrument valid between the parties thereto, in pursuance of which possession of the property is taken for foreclosure.

That the Worcester Motor Co. Inc. was not insolvent at the time it executed the trust receipts, and the defendants did not have reasonable cause to believe that the company was insolvent.

Established Facts.

The following facts, which negative any claim of a voidable preference, are established by the evidence:

1. The Worcester Motor Co. Inc. was not insolvent at the time it made a transfer of the motor vehicles to the defendants.

2. The defendants did not have any reasonable cause to believe that Worcester Motor Co. Inc. was insolvent at the time of the transfers.

3. The transfers of the motor vehicles were made for a present fair consideration.

4. The estate of Worcester Motor Co. Inc. was not depleted by the transfers of the motor vehicles which were bought at the time of transfer with the moneys advanced by the defendants.

5. The transfer of title to the motor vehicles by the execution and delivery of the trust receipts, followed by possession taken by the defendants in accordance with the provisions of the trust receipts and before bankruptcy, was

not null and void under the laws of Massachusetts as against creditors of the company, but was complete, lawful and effective.

6. The trust receipts were unquestionably valid under the laws of Massachusetts.

7. No rights of third persons were involved, and the trust receipts were not required to be recorded by the laws of Massachusetts to be valid between the parties thereto.

The recording statute is as follows:

General Laws of Massachusetts, Chapter 255, Section 1.

Mortgages of personal property shall, within fifteen days from the date written in the mortgage, be recorded on the records of the town where the mortgagor resides when the mortgage is made, and on the records of the town where he then principally transacts his business. If the mortgagor resides out of the commonwealth, and the property mortgaged is within the commonwealth when the mortgage is made, the mortgage shall be recorded on the records of the town where the property then is. If a record in two different places is required and the mortgage is recorded in one within said fifteen days, it may be recorded in the other within ten days after the date of the first record. The mortgage shall not be valid against a person other than the parties thereto until so recorded; and a record made subsequently to the time limited shall be void. This section shall apply to bills of sale given for security, but shall not apply to assignments which transfer the title of a lessor or conditional vendor to a lease or other instrument containing a conditional sale agreement and to the personal property therein described. If the condition for redemption of the property included in such bill of sale is in writing, it shall be recorded with and as a part of the bill of sale; if the

condition for redemption is oral, a written statement of such condition signed by the mortgagee shall be so recorded.

Summary of the Argument.

1. There was no preference under the Federal Bankruptcy Act.
2. State or local law is decisive of the validity and legal effect of the trust receipts.
3. Under Massachusetts law the defendants had good title to the motor vehicles.
4. Conclusion.

Argument.

I.

THERE WAS NO PREFERENCE UNDER THE FEDERAL BANKRUPTCY ACT.

The record shows that Worcester Motor Co. Inc. was not insolvent at the time it transferred the motor vehicles to the defendants.

The insolvency of the debtor at the time of the challenged payment or transfer is an essential element of a voidable preference.

8 Corpus Juris Secundum 700.
Kaufman vs. Tredway, 195 U. S. 271.
Brislin vs. Killanna Holding Corp., 85 Fed. 2nd 667.
Ely vs. Greenbaum, 85 Fed. 2nd 501.
Doggett vs. Chelsea Trust Co., 73 Fed. 2nd 614.
Charlesworth vs. Hipsch Inc., 84 Fed. 2nd 834.
Certiorari Denied.

The test of insolvency as an element of a voidable preference is whether or not the property and assets of the debtor at a fair valuation are sufficient in amount to pay his debts.

8 Corpus Juris Secundum 701, 777, 831.

There was a present adequate and fair consideration paid when each trust receipt was executed. Security taken for bona fide cash advances to the bankrupt, even when he is insolvent, does not constitute a preference. There was no fraud or collusion. The defendants acted in good faith and within the powers given them under the trust receipts. The estate of Worcester Motor Co. Inc. was not diminished.

Humphrey vs. Tatman, 198 U. S. 91.
Thompson vs. Fairbanks, 196 U. S. 516.
Kaufman vs. Tredway, 195 U. S. 271.
N. Y. County National Bank vs. Massey, 192 U. S. 138.
Newport Bank vs. Herkimer Bank, 225 U. S. 178.
Sexton vs. Kessler & Co. Inc., 225 U. S. 90, 97.
Finance & Guaranty Co. vs. Oppenheimer, 276 U. S. 10, 12.
Taney vs. Penn. National Bank, 232 U. S. 174.
Bailey vs. Baker Ice Machine Co., 239 U. S. 268.
Lindley vs. Ross, 200 Fed. 733.
Coffey vs. Managed Properties, 85 Fed. 2nd 88.
Green vs. First Savings & Trust Co. of Tampa, 36 Fed. 2nd 680.
Morrison vs. Bay Parkway National Bank, 60 Fed. 2nd 41.
Beacon Trust Co. vs. Dolan, 27 Fed. 2nd 247.
Brown Shoe Co. vs. Carns, 65 Fed. 2nd 294.
Irving Trust Co. vs. Bank of America Natl. Assn., 68 Fed. 2nd 887.

First National Bank vs. Live Stock National Bank, 31 Fed. 2nd 416.
First National Bank of Pedricktown vs. Waddington, 51 Fed. 2nd 1052.
Doggett vs. Chelsea Trust Co., 73 Fed. 2nd 614.
Richardson vs. Germania Bank of City of N. Y., 263 Fed. 320.
Certiorari Denied, 252 U. S. 582.

No creditor of a bankrupt can demand that the estate of the bankrupt be augmented by the application to the general estate of the bankrupt of property which never rightfully belonged to the bankrupt.

Gorman vs. Littlefield, 229 U. S. 19.

The giving of security for a present loan does not effect a preference.

Dean vs. Davis, 242 U. S. 438.
N. Y. County National Bank vs. Massey, 192 U. S. 138.
Newport Bank vs. Herkimer Bank, 225 U. S. 178.
First National Bank vs. Live Stock Natl. Bank, 31 Fed. 2nd 416.
Beacon Trust Co. vs. Dolan, 27 Fed. 2nd 247.
Doggett vs. Chelsea Trust Co., 73 Fed. 2nd 614.
First National Bank vs. Waddington, 51 Fed. 2nd 1052.
Certiorari Denied, *Waddington vs. Pedrick,* 284 U. S. 678.

The rights of the trustee in bankruptcy are no greater than those of Worcester Motor Co. Inc. at the time of adjudication.

Security Warehousing Co. vs. Hand, 206 U. S. 415.
Bailey vs. Baker Ice Machine Co., 239 U. S. 268.
York Manufacturing Co. vs. Cassell, 201 U. S. 344.
Bryant vs. Swofford Bros., 214 U. S. 279.

The enforcement or satisfaction of a valid existing lien or security does not in general effect a voidable preference.

Humphrey vs. Tatman, 198 U. S. 91.
Thompson vs. Fairbanks, 196 U. S. 516.
Johnson vs. Root Mfg. Co., 241 U. S. 160.
Irving Trust Co. vs. Bank of America Natl. Assn., 68 Fed. 2nd 887.
Certiorari Denied, 292 U. S. 628.

Taking possession before bankruptcy of property covered by a valid chattel mortgage by the mortgagee for the purpose of perfecting his lien is not a preferential transfer.

Sexton vs. Kessler & Co. Inc., 225 U. S. 90.
Thompson vs. Fairbanks, 196 U. S. 516.
Fairbanks Shovel Co. vs. Wills, 240 U. S. 642.
Hurley vs. Atcheson, Topeka & Santa Fe Rwy., 213 U. S. 126.
Dale vs. Pattison, 234 U. S. 399.
In re: Hurley, 185 Fed. 851.
In re: Schilling, 251 Fed. 972.
In re: East End Mantle & Tile Co., 202 Fed. 275.
In re: Howard, 207 Fed. 402.
In re: Social Circle Cotton Mills, 213 Fed. 994.

II.

STATE OR LOCAL LAW IS DECISIVE OF THE VALIDITY AND LEGAL EFFECT OF THE TRUST RECEIPTS.

Whether or not the trust receipts or chattel mortgages must be recorded in order to be valid between the parties thereto under the provisions of Section 60 of the Bankruptcy Act depends upon the applicable State or local law.

8 Corpus Juris Secundum 737.
Martin vs. Commercial Natl. Bank of Macon, Ga., 245 U. S. 513.
Carey vs. Donohoe, 240 U. S. 430.
Hartford Accident & Indemnity Co. vs. Coggin, 78 Fed. 2nd 471, Certiorari Denied, 296 U. S. 620, Rehearing Denied, 296 U. S. 663.

The legal effect of the transaction depends upon the local law.

Taney vs. Penn Bank, 232 U. S. 174.
Thompson vs. Fairbanks, 196 U. S. 516.
Humphrey vs. Tatman, 198 U. S. 91.
York Mfg. Co. vs. Cassel, 201 U. S. 344.
Hiscock vs. Varick Bank, 206 U. S. 28.
Security Warehousing Co. vs. Hand, 206 U. S. 415.
Bryant vs. Swofford Bros., 214 U. S. 279.
Holt vs. Crucible Steel Co., 224 U. S. 262.
Dooley vs. Pease, 180 U. S. 126.
Dale vs. Pattison, 234 U. S. 399.
In re: Harvey, 212 Fed. 340.

III.

Under Massachusetts Law the Defendants Had Good Title to the Motor Vehicles.

The transfer of the motor vehicles to the defendants by means of the trust receipts executed by the Worcester Motor Co. Inc. was valid under State law. Trust receipts are governed by the same rules as chattel mortgages. They are valid as between the parties thereto whether recorded or not. Upon repossession before bankruptcy and before any third persons had intervened the defendants perfected their title. They acted in good faith and did not receive any more than was due them. The estate of Worcester Motor Co. Inc. was not diminished by the defendants. The motor vehicles were purchased with their money; the invoices with the trust receipts given them. The transfer was thus made for a present and adequate consideration and at a time when the Worcester Motor Co. Inc. was solvent.

Mason vs. Wylde, 1941 Mass. Advance Sheets 367.

It is the settled law of this Commonwealth that an instrument of transfer of personal property absolute in form, but intended by the parties to be a mortgage, genuine, honest and valid as such when executed and delivered, authorizes the person named as vendee to take possession of the property in order to secure his own debt at any time before the rights of other persons have intervened, and that thereby he acquires a title which relates back for its validity to the date of the instrument, and that although the taking possession may be at a time when the debtor is insolvent to the knowledge of himself and of his creditor named as vendee in the instrument of transfer, it is, never-

theless, effectual although occurring within a period of time previous to insolvency which would vitiate the transaction if the initial step had occurred at the time of taking possession.

Coggan vs. Ward, 215 Mass. 13.

There is no question that a chattel mortgage is valid between the parties though not recorded.

Dale vs. Pattison, 234 U. S. 399.
McGlue vs. Loudon, 251 Mass. 173.
Arnold vs. Chandler Motors, 244 Mass. 210.
Atlantic Transportation Co. vs. Alexander Shipping Co., 261 Mass. 1.
Carey vs. Donohue, 240 U. S. 430.
Martin vs. Commercial National Bank, 245 U. S. 513.
Hartford Accident & Indemnity Co. vs. Coggin, 78 Fed. 2nd 471.

The omission to record the trust receipts did not affect their validity or limit the rights of the defendants. It is conclusively shown that they were valid as between the parties—the Worcester Motor Co. Inc. and the defendants. No creditor acquired a lien upon the property. The title of the defendants was perfected when they terminated the trust and took possession of the motor vehicles. After repossession they held the cars as their own property, not as security for debt.

Humphrey vs. Tatman, 198 U. S. 91.
Fairbanks Shovel Co. vs. Wills, 240 U. S. 642.
Thompson vs. Fairbanks, 196 U. S. 517.
Security Warehousing Co. vs. Hand, 206 U. S. 415.
Taney vs. Penn National Bank, 232 U. S. 174.

Finance & Guaranty Co. vs. Oppenheimer, 276 U. S. 10.
In re: Schilling, 251 Fed. 972.
Blanchard vs. Cooke, 144 Mass. 207, 223.
Cottrell vs. Carter Rice & Co., 173 Mass. 155.
Wasserman vs. McDonnell, 190 Mass. 326.
Arnold vs. Chandler Motors, 244 Mass. 210.
Mulloney vs. Black, 244 Mass. 391.
Vorenberg vs. American House Hotel Co., 246 Mass. 108.
Alexander vs. F. L. Smithe Machine Co., 248 Mass. 436.
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Atlantic Transportation Co. vs. Alexander Shipping Co., 261 Mass. 1.
Hanford vs. Codman, 266 Mass. 93.
Ferguson vs. Winchester Trust Co., 267 Mass. 397.
Harris vs. Flynn, 272 Mass. 8, 14.
Mason vs. Wylde, 1941 Mass. Advance Sheets 367.
Bennett vs. Bailey, 150 Mass. 257.
Oshry vs. Haddad, 265 Mass. 199.
Comparone vs. M. J. Kaplan Co. Inc., 270 Mass. 74.
Baker vs. Chisholm, 268 Mass. 1.
Williams vs. Whitinsville Savings Bank, 283 Mass. 297.

The defendants acted in good faith. There was no fraud. They advanced money to the Worcester Motor Co. Inc. to enable it to purchase motor vehicles. There was no preference. Worcester Motor Co. Inc. was then solvent. The defendants perfected their title by repossession before bankruptcy and before any third persons intervened. They received no more than was justly due them.

At the time of the bankruptcy Worcester Motor Co. Inc. did not own the motor vehicles, and the trustee in bankruptcy is vested with no better right or title than the bankrupt had when the trustee's title accrued.

Bailey vs. Baker Ice Machine Co., 239 U. S. 628.
York Mfg. Co. vs. Cassel, 201 U. S. 344.
Bryant vs. Swofford Bros., 214 U. S. 279.
Kaufman vs. Tredway, 195 U. S. 271.
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Comparone vs. M. J. Kaplan Co. Inc., 270 Mass. 74.
Shay vs. Gagne, 275 Mass. 386.
Barishefsky vs. Cohen, 299 Mass. 360.
Kerrigan vs. Fortunato, 304 Mass. 617.
Mason vs. Wylde, 1941 Mass. Advance Sheets 367.

Worcester Motor Co. Inc. was bailee of certain motor vehicles, the title to which was in the defendants. It agreed to hold the motor vehicles in trust for the defendants, to preserve the defendants' title intact, and to return them to the defendants on demand. The defendants had the right to terminate the bailment at any time.

A party holding security does not create a preference by taking possession under it within four months if he lawfully may under the law of the State.

Finance & Guaranty Co. vs. Oppenheimer, 276 U. S. 10, 12.

IV.

Conclusion.

The suggestion that the Bankruptcy Act and the State recording statutes, declaring valid as between the parties thereto an unrecorded chattel mortgage given by a solvent debtor for a fair, adequate and present consideration within four months prior to bankruptcy and foreclosed before any rights of third persons have intervened and before bankruptcy, may defeat the just claims of creditors and permit an unknown creditor to spring up just prior to bankruptcy armed with a hidden chattel mortgage and seize the very property which formed the basis for the creditor's lending money to the now bankrupt debtor, is purely gratuitous and wholly unsupported by the law or facts of the case at bar. The petitioner failed to prove his charges of conversion, preference, intent to hinder and delay, and moneys had and received.

The respondents respectfully ask that the petition for a writ of certiorari be denied.

Respectfully submitted,

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